

IN THE HIGH COURT OF GUJARAT AT AHMEDABAD

INCOME TAX REFERENCE No 259 of 1983

For Approval and Signature:

Hon'ble MR.JUSTICE R.K. ABICHANDANI and

Hon'ble MR.JUSTICE R.BALIA.

=====

1. Whether Reporters of Local Papers may be allowed to see the judgements?
2. To be referred to the Reporter or not?
3. Whether Their Lordships wish to see the fair copy of the judgement?
4. Whether this case involves a substantial question of law as to the interpretation of the Constitution of India, 1950 of any Order made thereunder?
5. Whether it is to be circulated to the Civil Judge?

-----

AIMS OXYGEN PVT LTD

Versus

COMMISSIONER OF INCOME TAX

-----

Appearance:

MR JP SHAH for Petitioner

MR BJ SHELAT FOR MANISH R BHATT for Respondent No. 1

-----

CORAM : MR.JUSTICE R.BALIA.

Date of decision: 10/01/97

ORAL JUDGEMENT

(per Rajesh Balia, J)

1. At the instance of the assessee, following question of law has been referred to this Court for its opinion which is arising out of Tribunal's order in ITA No.1023/Ahd/80 for the assessment year 1976-77:

"Whether, on the facts and in the circumstances of the case the Tribunal was right in law in disallowing Rs.71,000/- paid to Director Smt. Pravinaben?"

2. The facts relevant for the present purpose as appearing from Statement of Case and at annexures forming part of it may be noticed. Smt. Pravinaben Patel was Managing Director of the assessee company upto 30.4.1973. During the period of her continuation as Managing Director, she was being paid remuneration at the rate of Rs.1000 per month. She had also withdrawn certain amounts from the company which she claimed to be remuneration payable to her. It is also apparent that disputes had arisen between the management of assessee company and the sister concern Ashok Brothers Private Limited, Bombay which resulted in Company Petition No.13 of 1973 before this Court. One of the dispute before the court in the aforesaid company petition was about the claim of Pravinaben to the amount withdrawn by her from the books of the company as part of remuneration payable to her as Managing Director of the company which the company has declared to be payable to said Pravinaben inter alia on the ground that Managing Director's remuneration was only Rs.1000/- per mensem and anything beyond it are referable to the advance withdrawals made by said Pravinaben which are liable to be recovered by the company. That dispute was settled by company deciding not to recover the said amount and Pravinaben agreeing not to claim any additional sum other than Rs.71,000 by way of remuneration.

3. The assessee claimed a deduction of Rs.71000 from its income chargeable to tax under the head Profits and Gains from Business and provision for the assessment year 1976-77 as a business expense. The assessee's claim was primarily under Section 37 of the Income Tax Act as an expense exclusively and wholly laid out for the purpose of business. Alternatively, it has also been claimed that it is allowable as an expense under Section 28 for finding out the net profit of the company. The Income Tax Officer came to the conclusion that Rs.71000 represent the withdrawal of director's remuneration which should have been claimed in the relevant assessment years in which Pravinaben has withdrawn the amount and was not liable to be considered during the assessment year in question. On further appeal, the CIT (Appeals) observed that Smt. Pravinaben was not a Director during the year under appeal that is assessment year 1976-77 and hence the question of giving her any remuneration did not

arise. As a result of this finding the order of Income Tax Officer was confirmed. On further appeal, Tribunal gave a finding that the remuneration was not payable to the lady as she was not a Director at any time during the accounting year and secondly that the claim of allowance of Rs.71000 under Section 28 or Section 37 is essentially based on the ground that consent decree passed by the High Court which amounts to settlement where some parties relinquish some rights to settlement and some rights in return of getting some other rights, therefore, this decree for not recovering the sum of Rs.71,000 from the lady was overall settlement. The agreement was not an agreement to pay Rs.71000 to the lady. On the basis of these reasonings the view taken by the CIT (Appeals) was confirmed.

4. The assessee has laid his claim to allowance on two alternative grounds. Firstly, that his agreeing not to recover the amount of Rs.71000 resulted in writing off of the company's dues and amounted to an expense which was laid out wholly and exclusively for the purpose of carrying out the business. Alternatively, he has claimed that if the amount to be adjusted as part of remuneration paid to the Managing Director while computing the net profit of the business of the company, it be allowed as part of the cost of running the business.

5. So far as the alternative ground of the claim to deduction by the assessee is concerned, there does not appear to be much complicity. During the period upto which said Pravinaben was held to be director of the company, the payment made to her as director's remuneration during that relevant period had been considered by the assessing authorities and to the extent it was found allowable in terms of Section 40(c) of the Act, the same had been allowed. Any amount paid in excess of the sum held by the assessing authorities to be allowed under Section 40(c) for that period cannot obviously be considered for allowance as remuneration paid to the directors for that year. This position we find from para 9 of the Tribunal's order was also not seriously disputed by the learned counsel for the assessee before the Tribunal.

6. However, the claim of the assessee about the deduction of the sum which he has agreed not to recover from Smt. Pravinaben which according to its books of accounts was recoverable from her does not admit of such simple solution. It cannot be doubted that for treating a sum to be as an allowable deduction as an expense incurred or laid out wholly and exclusively for the

purpose of carrying on business need not in all cases be actual payment. It may be in the shape of a business loss arising out of normal hazards of carrying on business. For example, embezzlement by a cashier of the person carrying on business of finance or a debt which has become irrecoverable, or it may be actually incurred by actual payment. Therefore the fact that no actual payment was envisaged under the settlement of dispute between Pravinaben and the company, vis-a-vis the amount of Rs.71000 is of little relevance. So also whether the settlement of not to recover Rs.71000 from Smt. Pravinaben was a result of over all settlement between parties or a settlement of single dispute cannot be of a decisive relevance for the purpose of finding out whether foregoing a claim to recover Rs.71000 was as a result of commercial expediency so as to treat as an expense laid out wholly and exclusively for the purpose of business or not. It is of still little consequence whether such settlement was arrived at as a result of adjudication by an adjudicating agency or through settlement during the course of litigation pending before the court, or even before going to the courts at all. The real question which requires determination in such case is whether decision of the company not to recover Rs.71000 from Smt. Pravinaben, its erstwhile director with whom it had certain disputes was an outcome of existence of commercial expediency which could be reasonably taken into consideration by an ordinary prudent businessman, or the decision was de hors the consideration of its carrying on of the business. The question whether the decision not to recover the amount from the lady was a decision taken by the management of the company for the purposes of carrying on its business as a measure of commercial expediency or not is essentially a finding of fact which the Tribunal ought to have decided. However, from the order of the Tribunal we find that the Tribunal has not adverted to this aspect of the case at all and has not recorded any finding notwithstanding that assessee had raised the issue for basing his claim under Section 37 of the Act. It appears that the Tribunal was duly influenced by the fact that no amount was in fact paid during the previous year in question and no remuneration was payable for that assessment year and that the amount has been decided to be not to be recovered as a result of consent decree and not by way of any adjudication. Precisely for the reason that the question about the claim of Pravinaben as refuted by the company about anything to be payable towards remuneration having not been decided it became imperative for the Tribunal to have found out the real nature of the transaction of settlement, namely, whether it was

prompted by commercial consideration or some other consideration. In the absence of basic finding by the Tribunal, which is a final fact finding authority, it is not possible to answer the question referred to us.

7. Under the circumstances, two options are open to us either to direct the Tribunal to decide this question and submit a supplementary statement of case or to decide the issue afresh in accordance with law. In the circumstances, we deem it proper to adopt the latter course by refusing to answer the question and directing the Tribunal to decide the real issue about the nature of it foregoing recovery of it against said Smt. Pravinaben under the said settlement for the purpose of deciding its allowability as deduction under Section 37 of the Act.

Reference accordingly stands disposed of. No order as to costs.